



Chinese-led Special Economic Zones in Africa: problems on the road to success

The success of Chinese-led SEZs in Africa is important to both the Chinese government and the host governments. Even though these zones are operating under market conditions, the role of both sides in creating effective institutional arrangement for SEZs is crucial. The Chinese-led SEZ programme was initiated in 2006 and 2007, and was intended to be implemented before 2009. Even though the Chinese government and host governments showed their willingness to push forward SEZ programmes vigorously, most of them have not materialised yet. Most of the SEZs have been under construction and are not yet operating. This paper first provides the brief background of the establishment of SEZs in Africa, then the focus moves to stakeholders involved in the programme. Finally, the paper explores the current situations and navigates the role of the host governments to make the SEZs work. To help the Chinese-led SEZs in Africa to become successful, the host governments must remain actively involved in the SEZs, because their support is more significant than any other aspect. Furthermore, they should provide consistent policies and effective incentives for the investors. On the other hand, the host governments should impose firm requirements in terms of technology transfer and basic working conditions so that their countries can reap the benefits of Chinese investment.

Special Economic Zones (SEZs) in Africa were one of the pledges of the Chinese government at the Forum on China-Africa Cooperation (FOCAC) summit held in Beijing in November 2006. While the Chinese government sought opportunities for Chinese enterprises abroad, the establishment of economic and trade cooperation zones was part of the Chinese government's "going out" policy which encourages and assists domestic companies in developing a global strategy to exploit opportunities in the new market. After a bidding process, Egypt, Ethiopia, Mauritius, Nigeria and Zambia were finally selected to host Chinese-led SEZs. Most of the zones have not reached their full potential yet since some of them are still under construction and most of them are only partially operating.

Since 2007 some progress has been made, starting with the Chambishi zone in Zambia. The Oriental zone in Ethiopia has recently started partial operation hosting a few manufacturing industries. Since the initiative was based on

China's own successful experience of SEZs, Chinese-led SEZs have attracted much attention and have become a testing ground for this new policy experiment. The success of Chinese-led SEZs is important for both China and for the African host countries. Chinese enterprises, which experience severe competition within China, can enter new markets. These markets are in African countries and beyond them, as SEZs benefit from trade preferences granted to host countries. Thus, country-of-origin labelling or the availability of a particular tariff preference programme might help Chinese enterprises access the US or the EU markets. These SEZ programmes are also hoped to establish a good image on the African continent, somewhat countering the image of a 'predator trade partner' seeking only natural resources. In this rationale, SEZs could – if successful – enhance its image as a benevolent partner and thus contribute to expanding China's soft power.

Box 1: Types of zones

There are various types of zones for different purposes such as export processing zones (EPZs), industrial development zones (IDZs), free zones, and industrial parks, among others. Especially, SEZs and EPZs are often used interchangeably. SEZs and EPZs are created by the governments with certain aims: 1) to attract the foreign investment 2) to develop infrastructure 3) to create jobs 4) to promote technology transfer. However, they differ in size, scope of business and objective and among others. EPZs are industrial estates aimed primarily at attracting export-oriented investments. SEZs are larger estates and usually cover all industrial and service sectors and target both foreign and domestic markets and generally open to all activities.

	EPZs	SEZs
Main goals	Promoting exports	Overall development of the zones
Main activities	Manufacturing and other related activities	All types of industry and services
Physical characteristics	Industrial park	Entire province, region or municipality
Infrastructure	Manufacturing units only	Manufacturing units, on/off site infrastructure and other services
Forms of Investment	Private foreign investors only	Local investors are involved

Source: Engman, M., O. Onodera and E. Pinali (2007), "Export Processing Zones: Past and Future Role in Trade and Development", OECD Trade Policy Papers, No.53, OECD Publishing.

SEZs are also expected to attract investment to the host countries and thereby help industrialisation, which, it is hoped, can contribute to diversification of the economies of African countries which are presently largely based on the extractive industry. The programmes are expected to stimulate the growth of host countries' competitiveness. Technology transfer and job creation are further expected benefits. It is especially hoped that host governments can resolve unemployment issues, which are often one of the causes for instability in a country.

Various actors are involved - but a lack of local involvement

There are four main actors involved in the Chinese-led SEZs in Africa. First of all, the Chinese government is one of the main drivers of the SEZ programme as they initiated the programme and provided financial and non-financial support for developers and investors. Various state agencies such as the Ministry of Commerce (MOFCOM) and the China-Africa Development Fund (CAD Fund) are involved in planning, promoting, marketing and attracting Chinese investors. MOFCOM is in charge of the bidding process, loans and subsidies. The CAD Fund, a government equity fund, plays a major role in promoting joint ventures involving Chinese and local investors.

The CAD Fund itself is the second largest shareholder in the Lekki Zone in Nigeria and the JinFei Zone in Mauritius. Other actors are the Export-Import Bank of China and Chinese provincial governments as well as Chinese State-Owned Enterprises.

Secondly, each zone operates under market mechanisms, it is important to scrutinise private and joint venture enterprises, because these Chinese private enterprises represent an increasing share of China's FDI to Africa. A World Bank study of January 2013 illustrates that Chinese private investment in Africa has outnumbered Chinese state-owned enterprises by taking up 55% of the total Chinese investment. Chinese local businesses face severe competition within China itself. Additional local pressure is coming from the rising costs of production in China due to increasing labour costs and commodity prices. Under these circumstances, the idea of relocating businesses to Africa might seem wise to private enterprises. Yet the private Chinese investors are not having an easy time accessing many of the incentives that investors in state-owned businesses possess despite the former's increasing involvement in businesses in Africa.

Against this background, Chinese companies moving into the zones are eligible for a number of incentives, including the reimbursement of moving expenses, tax rebates, and others.

In addition to these direct incentives, cheap and abundant labour and easy access to local and international markets seem to be particularly attractive to Chinese investors.

Thirdly, African host governments are supposed to play important roles. In reality, even though each host government has a different institutional environment, the host governments in general strive to create favourable environments for foreign investors. It has taken a long time for these SEZs to go into operation, which seems also to be related to a lack of push from the side of the host governments. However, except in the case of Nigeria, the host governments' share in the SEZ is usually relatively small with up to 5%, or even – as in the cases of Ethiopia and Mauritius – non-existent.

Lastly, local population is the major source of labour in the SEZs and thus a factor to consider. The SEZs have contributed to job creation but several problems are being experienced. These are often derived from the absence of related regulations in the host country itself, and the lack of skilled workers in the host countries. The first and foremost problems are related to minimum wages. Most workers earn less than the minimum wage they are entitled to. Most of the host countries have legal and regulatory frameworks but these are not full protection, not least so as the government implementation is inadequate.

The current situation regarding the Chinese-led SEZs in Africa

Most of zones have completed office buildings, internal roads, industrial and warehousing units. Their planned focus is on manufacturing, mainly light machinery and textiles. Chambishi is an exception to this: the zone was originally designed for copper and cobalt related industries as the zone lies in the Copper Belt. Some other countries such as Nigeria have modified their original plans, and are considering opening the SEZs to other sectors such as the service sector including property and banking. Since the first announcement of the establishment of zones, several problems in the operation have emerged. It is essential for host governments to design overarching schemes for SEZs, which need linkages to national development programmes in the first place. SEZ programmes will require enormous investment from the host governments, which makes the integration into long-term visions even more urgent. Host governments will, for instance, have to provide on/off site infrastructure, electricity and water connections. Cost-benefit analysis and calculations regarding the countries' own comparative advantages are thus advisable before the investments. It is also still unclear how SEZs in host

countries relate to each other. If there is no macro coordination, the risk is for SEZs to increase the competition with enterprises in the host countries.

Secondly the zones operate according to market mechanisms. Therefore, it is important to create a business friendly environment and set up institutional arrangement that can support investors. When a host country is seen as a high political risk, this discourages foreign investors and in order to secure investment, the host government has to compensate by making concessions.

Thirdly, and closely related to the second point: even though it is important to attract foreign investors' participation in the zones, local investors also need encouragement. Although most Chinese investors have enjoyed unprecedented support from both the Chinese side and the host governments, local businesses are, in most cases, excluded from incentives. In the case of Ethiopia, local businesses are not allowed to invest in the Chinese-led SEZs. There is thus a tendency to create SEZs as enclaves. Without spill-over from the zone, however, its implications will be limited. The Chinese domestic experiences show how important it is to synchronise the zone and local economy including local suppliers and local universities. One of the fundamental goals of FDI is to boost local competitiveness through active interaction with advanced foreign businesses. In this process, it is important to enhance and empower locals. Knowledge transfer only happens when the host countries' technology level is similar to that of the home country. At the moment, the trend seems to be that most companies are in the labour intensive sector, rather than in technology intensive sectors. Host governments need to be aware that investors can ultimately move their businesses to another country, if the alternative country can provide labour at a more competitive, lower cost. The exclusive reliance on cheap labour is a risky strategy, as this competitive advantage is easily lost. Host governments thus would need to continuously invest in human capital, upgrading the skills of labour.

Fourthly, inside the zones, the role of host governments is also significant. The host governments are responsible for monitoring the practice of investors. Issues regarding environment and labour practices have been pointed out as aspects that require special attention. However, in practice, these are often overlooked as host governments are usually more concerned about attracting foreign investors, not least so with a view to much needed job creation.

In many cases, labour regulations in SEZs are different from those in host countries, for example, often there exist no specific regulations with regard to minimum wages, leave, training, and the rights of the association of workers' unions.

Table 1: Investment structure of SEZs

Country / SEZ		Status as of early 2013	Ownership structure
Egypt	Suez	Operational	Tianjin TEDA, CAD fund, Egypt-china Corporation for Investment, Tianjin Suez International Cooperation share ownership
Ethiopia	Oriental	Operational	Consortium of Qiyuan Group, Jianglian and Yangyang Asset Management share ownership
Zambia	Chambishi	Operational	5% holding through Zambian state owned, Zambia Consolidated Copper Mines Investment Holdings
	Lusaka	Under construction	
Nigeria	Lekki	Under construction	China-Africa Lekki Investment Co. Ltd 60% (a consortium of four Chinese companies) Lagos State Government 20%, Lekki Worldwide Investment Ltd 20% (owned by Lagos State Government)
	Ogun-Guangdong	Operational	Ogun State Government 18%, Consortium of Guangdong Xinguang International Group, and China-Africa. Investment Ltd and CCNC Group 82%
Mauritius	Jin Fei	Completed construction, not operating yet	Taiyuan Iron and Steel 34%, Shanxi Coking Coal 21%, Tianli Enterprises Group 12.5% and CAD fund 32.5%

Source: Bräutigam, D. and Tang, X. (2011) 'African Shenzhen: China's special economic zones in Africa', *Journal of Modern African Studies* 49 (1): 27-54.

This tendency is often described as a race to the bottom, lowering the living standards of the people in the host countries, if competition is with economic activities outside the SEZ.

Conclusions and Recommendations

The success of the SEZs depends on the conducive business and operational environment. In this regard the host government is the most significant actor in the project; as per usual, development cannot be simply imported. SEZs should be seen as experiments, i.e. successful elements are continued and enlarged, whereas unsuccessful approaches are changed or abandoned; they are no panacea for or shortcut to development. This should be properly communicated to avoid frustrations. Indeed, SEZs need some time before they can contribute to the host country's economy. Even in the case of China in the 1980s, the contribution of SEZs to the Chinese economy was only 1% of China's GDP, but only since the early 1990s, the programme has led to an increase in FDI.

Learning and adjustments will have to be given a chance. Also, African host governments should put their local investors as a top priority and have a long-term strategy in

place of which SEZs form an integral part, rather than rushing to create enclaves for foreign investors. The fundamental goal of the establishment of SEZs is to improve the general investment conditions in African countries and this will take place when the host government has better infrastructure and technology, and educated and competent labour – and will need to keep an eye on implementation at lower administrative levels. The key to success is in the hands of the host governments.

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